
SENATE COMMITTEE ON GOVERNANCE AND FINANCE

Senator Mike McGuire, Chair
2019 - 2020 Regular

Bill No: SB 1300
Author: Skinner
Version: 5/22/20
Consultant: Peterson

Hearing Date: 5/28/20
Tax Levy: No
Fiscal: Yes

REDEVELOPMENT AGENCY DISSOLUTION: FINDING OF COMPLETION: CITY OF HERCULES

Allows the redevelopment successor agency in the City of Hercules to receive a Finding of Completion from the Department of Finance.

Background

Redevelopment agencies. From the early 1950s until the state dissolved them in 2011, California redevelopment agencies (RDAs) used property tax increment financing to pay for economic development projects in blighted areas. Generally, property tax increment financing involves a city or county forming a tax increment-financing district to issue bonds and use the bond proceeds to pay project costs within the boundaries of a specified project area. To repay the bonds, the district captures increased property tax revenues generated when projects financed by the bonds increase assessed property values within the project area. To calculate the increased property tax revenues captured by the district, the amount of property tax revenues obtained by any local agency that receives a share of property tax revenues from property within a project area is “frozen” at the amount it received from that property prior to the project area’s formation. In future years, as the project area’s assessed valuation grows above the frozen base, the resulting additional property tax revenues—the increment—flows to the tax increment financing district instead of other local agencies. After the bonds have been fully repaid, the district is dissolved, ending the diversion of tax increment revenues from participating local agencies. Property tax revenues then flow back to each local agency that receives a share of the property tax.

Citing a significant State General Fund deficit, Governor Brown’s 2011-12 budget proposed eliminating RDAs and returning billions of dollars of property tax revenues to schools, cities, and counties to fund core services. Among the statutory changes that the Legislature adopted to implement the 2011-12 budget, AB X1 26 (Blumenfield, 2011) dissolved all RDAs. The California Supreme Court’s 2011 ruling in *California Redevelopment Association v. Matosantos* upheld AB X1 26, but invalidated AB X1 27 (Blumenfield, 2011), which would have allowed most RDAs to avoid dissolution. In response, the California Redevelopment Association (CRA) challenged the two measures. The Supreme Court denied the petition for peremptory writ of mandate with respect to AB X1 26, but granted it with respect to ABX1 27. As a result, all RDAs dissolved as of February 1, 2012. At the time of dissolution, over 400 RDAs statewide were diverting 12% of property taxes, over \$5.6 billion yearly.

RDAs' dissolution deprived many local agencies of the primary tool they used to eliminate physical and economic blight, finance new construction, improve public infrastructure, rehabilitate existing buildings, and increase the supply of affordable housing. Until their dissolution, state law required RDAs to set aside 20% of funding generated in a project area to increase the supply of low- and moderate-income housing. At the time the state dissolved RDAs, the Controller estimated that statewide, RDAs were obligated to spend \$1 billion on affordable housing.

RDA dissolution. AB X1 26 (2011) established successor agencies to manage the process of unwinding former RDA affairs. With the exception of seven cities, the city or county that created each former RDA now serves as that RDA's successor agency. One of a successor agency's primary responsibilities is to make payments for the enforceable obligations RDAs entered into. These payments are supported by property tax revenues that would have gone to RDAs, but are instead deposited in a Redevelopment Property Tax Trust Fund (RPTTF). Enforceable obligations include bonds, bond-related payments, some loans, payments required by the federal government, obligations to the state or imposed by state law, payments to RDA employees, judgements or settlements, and other legally binding and enforceable agreements or contracts. Any remaining property tax revenues that exceed these enforceable obligations return to cities, counties, special districts, and school and community college districts to support core services.

If those school districts were nonbasic aid districts, meaning they need both local property tax revenue and State General Fund revenue to meet their minimum funding guarantee, the State General Fund backfills these school districts' revenues with more General Fund revenue if the districts did not receive enough local property tax revenue to meet their minimum funding guarantee. Absent changes to existing law, the State General Fund is expected to offset at least \$2 billion in property tax revenues diverted from K-14 schools through 2022-23 as a result of ongoing redevelopment dissolution. Some of the State General Fund offset will continue until all redevelopment obligations are paid off. The level of offset beyond 2022-23 will depend on property tax growth and the remaining RDA obligations.

Each successor agency has an oversight board responsible for supervising and approving its actions. The Department of Finance (DOF) can review and request reconsideration of an oversight board's decision. Once a successor agency takes over for an RDA, it reviews the RDA's outstanding assets and obligations, and develops a plan to resolve those obligations, also known as a Recognized Obligation Payment Schedule (ROPS). To obtain required DOF approval, a successor agency submits a series of ROPS to the department. If DOF agrees with the plan, it issues a Finding of Completion acknowledging their progress towards paying off their obligations. Successor agencies issued a Finding of Completion can submit a Last and Final ROPS, meaning that (1) the remaining debt is limited to administrative costs and payments pursuant to enforceable obligations with defined payment schedules, (2) all remaining obligations have been previously listed on the ROPS and approved by DOF, and (3) the agency is not a party to outstanding or unresolved litigation. Successor agencies had until December 31, 2015 to receive their Finding of Completion from DOF. RDA dissolution law states that successor agencies that did not receive their Finding of Completion by this date, or did not enter into a written installment payment plan with DOF, were to never receive a Finding of Completion. Nine successor agencies did not receive a Finding of Completion by the deadline.

If a successor agency receives a Finding of Completion, loan agreements made between the RDA and the local agency that created it can become enforceable obligations. Without a Finding of Completion, these loans cannot become enforceable obligations and the successor agency cannot repay the loans with property tax revenue. Additionally, successor agencies with a Finding of Completion can spend a greater portion of bond proceeds in excess of what is necessary to pay off enforceable obligations provided they remain consistent with bond covenants, not just to cancel or defease the bonds. When bond proceeds are defeased or cancelled, property tax revenue used to pay off bonds returns to the local agencies that generated the property tax revenue, not the RPTTF.

City of Hercules. The City of Hercules, a city of over 25,000 people in Contra Costa County, is one of the nine successor agencies without a Finding of Completion. According to the City, RDA dissolution coincided with a period of financial challenges, including financial impacts from the Great Recession and a corrupt city manager. In September 2012, the State Controller reviewed the financial transactions of the Hercules RDA and found serious mismanagement practices by the former City Manager/RDA Executive Director. The City has spent the better part of the last decade recovering from these fiscal challenges, which made it difficult to meet the 2015 deadline to receive a Finding of Completion.

The City of Hercules estimates that it has \$233.5 million in outstanding RDA obligations, including:

- \$151 million in outstanding bonds;
- \$58.7 million agreement with Catellus, a private company who agreed to clean up a former refinery and convert the property into housing, where the RDA promised a portion of future tax increment; and
- \$8.3 million in loan agreements between the City and its RDA for various projects, including infrastructure, park improvements, and debt service payments. The City does not anticipate that DOF would consider the remaining \$41.7 million in similar loans as enforceable obligations.

While the annual bond payments and the agreement with Catellus have previously been considered enforceable obligations and must be paid before other obligations, the loan agreements with the City cannot become enforceable obligations, and be repaid with property tax revenue, without a Finding of Completion.

On March 19, 2020, DOF and Hercules settled their remaining lawsuit. As part of the settlement, the City entered into a written payment plan that requires them to pay the State \$3.6 million in four payments over a three-year period. The City has already made one of these payments, and the next payment is due May 1, 2021.

Now that the City of Hercules has developed a payment plan with DOF, the City wants a Finding of Completion to refinance its RDA obligations even though the deadline has passed.

Proposed Law

Senate Bill 1300 would allow DOF to issue a Finding of Completion to the successor agency in the City of Hercules despite missing the December 31, 2015, deadline, so long as it enters into, and follows, a written installment payment plan with DOF.

State Revenue Impact

No estimate.

Comments

1. Purpose of the bill. According to the author, “SB 1300 is a district bill that allows the Department of Finance to issue a final notice of completion for redevelopment dissolution to the City of Hercules after the current statutory deadline as long as they have paid or legally agreed to pay any amount owed to the state as a result of the dissolution of their redevelopment district. Given the economic downturn caused by the pandemic and the resulting impact on many local governments’ budgets, this bill by providing a final notice of completion will assist Hercules clear up ownership and title issues and facilitate refinancing, prepayment and other actions that are estimated to generate additional income.”

2. No free lunch. AB X1 26 created successor agencies to unwind RDA obligations so that property tax revenues previously going to RDAs flow back to the local agencies generating the revenue. Importantly, school districts and community college districts are also affected, which impacts the state by way of the Proposition 98 minimum funding guarantee. If the City’s successor agency receives a Finding of Completion, it would have access to the same benefits as other successor agencies that already received one, including (1) using excess bond proceeds for other purposes, and (2) considering some loan agreements between the City and the RDA as enforceable obligations. Either action could deprive other affected taxing entities agencies and the State General Fund of future property tax revenues because those revenues will instead flow to the successor agency for a longer duration, which adds to the ongoing costs of winding down redevelopment that the state and local agencies must already bear. While the City does not plan to change how it spends bond proceeds, it does anticipate classifying \$8.3 million in loans between the City and the RDA as enforceable obligations. Using \$8.3 million to pay off the loan with the City would require up to \$4.9 million dollars from the State General Fund, because the schools’ share of property tax revenue in Contra Costa County is 59%, and \$3.4 million from other affected taxing entities. These amounts could be higher if more loans qualify as enforceable obligations. The Committee may wish to consider whether the State General Fund and other taxing entities should support a city that was unable to meet the deadlines almost all other RDAs were able to meet.

3. A herculean task. Despite the costs to affected taxing entities described above, the City of Hercules believes that these entities would benefit from it receiving a Finding of Completion because they plan to refinance existing obligations at lower rates. While existing law allows successor agencies to refinance these obligations regardless of whether they have a Finding of Completion, the City contends that it would have to include the lack of a Finding of Completion in financial disclosure documents, which could make refinancing more complicated and expensive. The City estimates that refinancing existing obligations with a Finding of Completion, including the \$151 million in outstanding bonds and the \$58.7 million agreement with Catellus, could save up to \$44.5 million, including State General Fund savings up to \$26.8 million after accounting for the costs described above. Such estimates largely depend on the terms any refinancing agreements receive and whether that refinancing actually occurs. The bill does not actually require the City’s successor agency to refinance its existing obligations once it

receives a Finding of Completion. For these reasons, the level of savings the City might achieve is subject to some uncertainty. The Committee may wish to consider whether the bill provides enough assurance that the potential benefits from refinancing certain obligations outweigh the costs described above.

4. Late bird gets the worm? RDA dissolution law is explicit that successor agencies who did not receive their Finding of Completion by December 31, 2015, were never to receive one. SB 1300 goes against the clear precedent by offering Hercules this opportunity. Additionally, DOF has not affirmed that it would grant a Finding of Completion to such a successor agency even if it has the authority to do so. The Committee may wish to consider whether the City of Hercules should enjoy the same benefits as other successor agencies given it missed the statutory deadline, pursued litigation against the State, and the precedent it would set for the remaining eight successor agencies without a Finding of Completion.

Support and Opposition (5/26/20)

Support: City of Hercules (sponsor).

Opposition: Unknown.

-- END --